

August 2, 2005
Docket 05-192

Comments submitted by The Heartland Institute on the proposed acquisition of Adelphia Communications by Comcast and Time Warner

The Heartland Institute is a non-profit, non-partisan policy research organization based in Chicago. Heartland's mission is to help build social movements in support of ideas that empower people. Such ideas include market-based approaches to telecommunications policy and deregulation in areas where property rights and markets do a better job than government regulation.

The Heartland Institute is filing comments in support of expeditious Federal Communications Commission review and approval of the proposed acquisition of the assets of Adelphia Communications Corp. by Comcast Corp. and Time Warner Inc. We believe this agreement is in the public interest.

Adelphia is in the midst of a Chapter 11 reorganization. Although the company has overcome a major financial and legal crisis that began in 2002 when the SEC began an investigation into the dealings of the company and its founders, the Rigas family, it is by no means in a condition to stand by itself.

Its current management has reorganized the company in an attempt to meet debt obligations as well upgrade Adelphia's cable TV infrastructure and operations to where they are on a par with the rest of the U.S. cable industry.

That job will not be completed without bringing the resources of larger, healthier companies to bear; the ultimate sale of the Adelphia properties has been an objective of the new management since the outset of the Chapter 11 process.

Adelphia is a weak company

While the proposed agreement might raise concerns about cable industry consolidation, we believe those concerns are misplaced. Objections on these grounds would have more validity if the merger partners were two large, healthy, vigorous competitors that face off in the same local markets. The Adelphia deal represents splits up a severely weakened company that would likely be unsuccessful on its own.

Comcast and Time Warner Inc.'s Time Warner Cable unit¹, as new owners of the Adelphia properties, are in a position to infuse cash, speed technology development and meet the demands of Adelphia's creditors. The Adelphia franchises will be transferred to experienced Multiple System Operators (MSOs). This assures a degree of seamless continuity for Adelphia customers and employees. Creditors are likely to be paid full value on outstanding debts.

In terms of serving the public interest, this is the best alternative of those facing Adelphia. Without this sale, or a sale like it involving another large cable company, Adelphia likely would go into receivership. Its cable properties would be sold off piecemeal, at greater uncertainty for Adelphia customers, a greater cost for Adelphia shareowners, and greater loss for Adelphia creditors, which might only see a fraction of their receivables paid in such a case. Even in such a "fire sale," Comcast and Time Warner Cable would likely be among the bidders, although the opportunity to craft an arrangement that leverages the respective cable companies' geographic footprints, as it is the case now, would be lost. There would be far more employee disruption. Adelphia customers in some areas might be orphaned if no buyer was interested in those particular properties as stand-alone systems.

The other alternative scenario is acquisition of Adelphia by a bank or other financial institution, or by an investment consortium. While such a purchaser might be financially sound, it will bring little or no experience of the cable business to bear. In fact, such a consortium will likely simply act as a third party agent of dissolution, and begin the process of sale of assets, much in the same way current Adelphia management is doing. Such an arrangement only serves to extend the reorganization period. Again, the Adelphia properties would end up being redistributed among other leading cable franchises, although without the cohesion, continuity or value the Comcast-Time Warner proposal offers.

Issues of ownership concentration

To further answer concerns about whether this sale creates too much cable industry concentration, it should be noted that Adelphia ranks fifth among cable Multiple System Operators (MSOs) in size, with 5.3 million subscribers. Comcast is the largest of all cable with 21.5 million subscribers. Time Warner Cable ranks second with 10.9 million. Under the terms of the deal, Comcast

¹ Time Warner Cable is a business division of Time Warner Inc. Side-by-side, Comcast's cable business is larger than Time Warner's. Overall, Time Warner, as a diversified corporation is many times larger than Comcast.

is acquiring only 1.8 million Adelphia customers, roughly the equivalent of the Comcast's net gain in customers for all of 2004.²

Time Warner Cable, the smaller of the two cable companies, will gain almost twice as many customers from Adelphia as Comcast -- 3.5 million. The deal also includes system swaps between Comcast and Time Warner Cable. Not only will these swaps create better regional synergies—resulting in better customer service for Comcast, Time Warner and former Adelphia customers—they fulfill the FCC requirements as part of its approval of Comcast's acquisition of properties owned by AT&T Broadband, including the divestiture of certain Time Warner investments inherited by Comcast as part of that sale.

Even so, some may insist that one less cable company, no matter what its financial condition, is bad for consumers. We disagree. We urge the Commission to look at this acquisition in the context of today's intermodal competition for broadband and video services.

A growing pool of strong players

The pool of players seeking the consumer entertainment and telecommunications dollar is growing. Cable TV companies and phone companies are now competing head-to-head in most markets. Indeed, cable company investors see the biggest revenue growth coming from telephone service, not pay TV.³ Meanwhile, phone companies such as SBC Communications and BellSouth see their future growth anchored in IP Video and Video over DSL.⁴

While the Adelphia acquisition gives Comcast and Time Warner additional customers and greater economies of scale when it comes to technology and programming purchasing, it does not consolidate competitors in individual local franchise markets. Neither does it increase either company's market share in the local franchise markets they serve. To the contrary, by providing the Adelphia properties with badly needed investment dollars and concurrent financial stability, the deal actually serves to strengthen competition in local markets where Adelphia, because of its financial woes, had been failing to meet the aggressive challenge from well-heeled phone companies, ISPs and direct broadcast satellite services.

² Comcast had a net gain of 1.7 million customers in 2004, according to its 2004 Annual Report

³ Peter Grant, "Cable Companies Call Up New Growth Story," *The Wall Street Journal*, August 2, 2005, p. C1.

⁴ "The War of the Wires," *The Economist*, July 30-Aug. 5, 2004, p. 53

We do not believe that the Commission should put conditions on the approval of this deal. As part of the arrangement, Comcast is divesting all remaining holdings in Time Warner Cable. There appear to be no cross-ownership issues or anticompetitive problems. Rather, the deal ensures that when completed, distribution of the Adelphia properties will be complementary with the respective holdings of Comcast and Time Warner.

Given the evolution of competitive telecommunications and broadband service, and the fact that competitiveness and market share depends on fast innovation, speed to market and easy access to capital, the public interest is best served when local markets are served by a group of healthy, growing competitors, not a patchwork of ailing players unable to keep up with one dominant player.

Heartland encourages proper due diligence from the Commission in its review of the agreement, but believes prompt and expeditious approval is important to complete Adelphia's bankruptcy process, reimburse creditors, and to give former Adelphia customers access to advanced services. We urge the Commission to proceed confidently but with as little delay as possible.